

STRATEGIC BUSINESS PARTNERSHIPS

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INTRODUCING STRATEGIC BUSINESS PARTNERSHIPS

- During the past three decades, collaborative strategies in international business have gained popularity.
- Particularly in high technology industries, leading firms have increasingly used joint ventures, joint R&D, technology exchange agreements, direct minority investments, and sourcing relationships.

INTRODUCING STRATEGIC BUSINESS PARTNERSHIPS

- All these inter-firm relationships are short of complete merger, but deeper than arm's-length market exchanges.
- Such relationships involve mutual dependence and shared decision-making between two or more independent firms. When R&D is a focus of the partnership, universities and other research institutes may also participate.
- They are characterized as **strategic business partnerships (alliances)**.

INTRODUCING STRATEGIC BUSINESS PARTNERSHIPS

- Databases tracking strategic partnerships show that the rate of formation of such partnerships has accelerated dramatically since the late 1970s.
- This dramatic increase reflects non-equity agreements by and large. In contrast, equity based partnerships have kept a fairly low profile.
- Current conditions in the global economy make these alliances advantageous, perhaps necessary, for firm competitiveness in many industries.

EXAMPLES

STRATEGIC BUSINESS PARTNERSHIPS

- Xerox - EDS IT outsourcing
- Petrobras deep sea drilling
- Marriott Hotel / Tyson's Corner
- Ericsson - Intrakom digital telecom switches
- Petrole de France / Tierra del Fuego refinery
- Micronas - Nokia semiconductors

INTERNATIONAL STRATEGIC BUSINESS PARTNERSHIPS

Three major and inter-related factors have been driving the surge of international partnering.

■ Globalization

- Multinational companies have relentlessly pushed into new geographical and product markets.

■ Technological Change

- The pace of technological advance has accelerated, partly as a result of increasing competition through globalization.

■ The notion of “core competency”

- Increasing international competition and rapid technological advance have robbed firms of their ability to be self-sufficient in everything they do. The idea now is, do internally what you do best and outsource the rest through partnerships

DEFINITION: JOINT VENTURES

- In the mid-1980s, OECD defined **joint ventures** as activities “...in which the operations of two or more firms are partially, but not totally, functionally integrated in order to carry out activities in one or more of the following areas:
 - buying or selling operations;
 - natural resource exploration, development and/or production operations;
 - research and development operations;
 - engineering and construction operations”

DEFINITION: JOINT VENTURES

- In general, the motives for setting up a joint venture were understood to include:
 - using complementary technology or research techniques;
 - raising capital;
 - spreading the risks associated with establishing an enterprise in a new product or geographical area;
 - achieving economies of scale;
 - overcoming entry barriers to domestic and international markets; and,
 - acquiring market power.”

HISTORY OF JOINT VENTURES

- Up until the late 1970s, inter-firm cooperation was dominated by equity partnerships
- There were few exceptions, involving research consortia organized under government auspices in industrialized countries such as the Engineering Research Associations in Japan and several research consortia organized in the United States in the 1970s to tackle energy problems

HISTORY OF JOINT VENTURES

- Two important changes have taken place since the early 1980s in terms of inter-firm cooperation:
 - The extent of cooperation has increased very much resulting in big numbers of national and international partnerships
 - The organizational structure of cooperation has changed dramatically, reflecting the increasing importance of **organizational flexibility**. Non-equity partnerships are currently dominating the landscape

HISTORY OF JOINT VENTURES

- Consequently, the joint venture definition shown previously (requiring the establishment of a new entity separate from the parents) proved too rigid to be able to accommodate the rapidly growing variety of institutional mechanisms to transfer organizational and technological knowledge
- The need for a better definition was met with a broader concept: the concept of a strategic partnership (alliance)

DEFINITION: STRATEGIC BUSINESS PARTNERSHIPS

- A **strategic partnership** was defined by David Teece as a web of agreements whereby two or more partners share the commitment to reach a common goal by pooling their resources together and coordinating their activities.
- A strategic partnership denotes some degree of strategic and operational coordination and may include things such as joint research and development (R&D), technology exchanges, exclusionary market and manufacturing rights, and co-marketing agreements. Partnerships may, or may not, involve equity investments.

PRIVATE SECTOR INCENTIVES TO PARTNER

- Access product and financial markets;
- Share costs of large investments such as R&D;
- Share risk, reduce uncertainty;
- Access complementary resources and skills of partners, such as finance, complementary technologies;
- Benefit from research synergies;
- Accelerate return on investments through more rapid diffusion of assets;

PRIVATE SECTOR INCENTIVES TO PARTNER

- Deploy resources efficiently to create economies of scale, specialisation and/or rationalisation;
- Increase strategic flexibility through the creation and optimal exploitation of new investment options;
- Unbundle the firm's portfolio of intangible assets, and selectively transfer components of this portfolio;
- Co-opt competition;
- Attain legal and political advantages in host countries.

PRIVATE SECTOR INCENTIVES TO PARTNER

- More broadly, partnerships have such virtues as **flexibility, speed, informality, and economy**.
- They can be put together in little time and be folded up just as quickly.
- They can involve little paperwork. In comparison to market internalisation through mergers and acquisitions, a close analogy of partnerships would be “love affairs instead of marriages”.

STRATEGIC TRADE-OFF OF COLLABORATION

Regardless of the strategic goal, collaboration with another firm always implies a **trade-off** between:

- **greater access** - to markets, finance, other resources, capabilities; and
- **lesser control** - of strategic decision making, day to day management, technological and other kinds of knowledge.

PRIVATE SECTOR RISKS IN PARTNERING

The most serious potential **cost** of collaboration is the partial loss of control, including:

- Losing some control over strategic decisions
- Losing some control over the use of its technology
- Losing some control over its position in the market

Decreased control could invite opportunistic behaviour by one or more partners resulting, e.g., in the involuntary loss of technological and other knowledge.

PRIVATE SECTOR RISKS IN PARTNERING

Other potential **drawbacks** for individual firms are:

- Transaction costs due to
 - Increased management needs;
 - Diversion of managerial attention;
 - Employees need to be coached to the agreement;
 - Decisions and responsibilities are usually subject to negotiation.

- Lack of compatibility with core interests - e.g., locking the firm into a product/service standard that may not be in its best interest.